WATER AND WASTEWATER FINANCE RECOMMENDATIONS

Finance Work Group

Revised Final Draft from February 12, 2003 Meeting

1. The City's capital improvement program for water and wastewater facilities should advance the urban growth set forth in the City's adopted Comprehensive Plan. The water and wastewater capital improvements needed to support the 12 year urban growth shown in the adopted Comprehensive Plan can largely be accomplished through the use of revenue bond financing.

2. This potential bonding capacity assumes the following conditions:

   - Modifying the City's current bond issuance practices, i.e., long maturities;
   - A 7 percent increase in wastewater rates effective FY 2003-2004.
   - Systematic increases in utility user rates;
   - Implementing development impact fees; and,
   - Financial projections do not include inflationary cost increases.

3. The City of Lincoln has the potential bonding capacity to support long-term system replacement and upgrades and expansion of capital facilities for its municipal water and wastewater systems through a carefully managed issuance of additional revenue bonds.

4. The term (i.e., amortization period) for future revenue bonds should be changed to more closely reflect the economic life of assets financed. The financing term for future bond issues should be limited to a minimum of 15 years and a maximum of 30 years. Because previous bond issues financing long term assets were amortized over 20 years, this change will lower the average annual debt service for future revenue bonds while fully repaying the bonds within the estimated economic life of the capital improvements identified for this period.

   Changing market conditions may afford the City opportunities to structure debt financing to achieve lower overall costs. Subject to amortizing debt within the estimated economic life of assets, the City should take advantage of any opportunities to structure debt financing or refinancing to achieve the lowest possible overall cost. Combined debt service should be as level as practical to facilitate sound financial planning and stable utility rates.

5. The City should manage its total outstanding water and wastewater debt to maintain an overall average debt service coverage ratio* within a range of 1.65 to 1.75 percent. It is understood that at the time of issuance of any new debt, the debt service coverage ratio must be at least 1.25. Following the guidelines provided by the rating agencies for management, rates, governance, competition, economy, and so on may even enhance the rating of the water and wastewater systems.

6. The City should manage its water and wastewater systems to ensure that the current Public Works & Utility bond ratings of AA+ Standards & Poors and Aa2 from Moodys are maintained.

7. The issuance of substantial amounts of new water and wastewater revenue bonds with longer maturities over the next ten years could limit the City's future ability to issue similar bonds.

8. The City should embark upon a disciplined approach for systematically reviewing and adjusting water and wastewater utility rates. Based on current projections, annual rate increases of 3 to 5 percent should be adequate to finance growth needs during the assumed 12 year planning period. Rate increases are not proposed to occur in each fiscal year. Rate increases should be managed to provide sufficient funds for capital improvements without imposing unreasonable increased on rate payers. We recommend that annual increases not to exceed 5 percent in any given year.

9. The City should prepare a long-term financial plan and update this plan on an annual basis using the parameters set forth herein.

10. Periodically, the City may find it worthwhile to make a comparison of the City's overall utility rate burden with the overall utility rate burdens of the cities considered to be prime competitors for attracting new employers to determine if Lincoln is remaining competitive.

CAPITAL IMPROVEMENT SUMMARY FY 2003-4 through FY 2014-15	
WATER	$169 million
WASTEWATER	168 million
TOTAL	**$337 million**

∗ Debt service cover ratio is defined as: cash flow available for debt service divided by the annual debt service requirement (principal plus interest).

Cash Flow = Revenues, less Operation and Maintenance Expenses, plus Depreciation.

Revenues = Total Operating Revenues, plus interest income, plus tap fees, plus impact fees.

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